No. 22509

IN THE UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

FRANK J. EVANS and MARGUERITTE A. EVANS,

Petitioners

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent

ON PETITION FOR REVIEW OF THE DECISION OF THE TAX COURT OF THE UNITED STATES

BRIEF FOR THE RESPONDENT

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OPINION BELOW

The opinion of the Tax Court is reported at 48 T.C. 704.

JURISDICTION

This petition for review involves deficiencies in federal income taxes for the years 1962 and 1963 in the respective amounts of $41.21 and $1,089.35. (R. 90-91.) The taxpayer[1] and his wife filed joint income tax returns with the District Director at San Francisco, California. (R. 67.) On March 11, 1966, the Commissioner mailed a

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1/ For convenience, Frank J. Evans will be referred to in this brief as the taxpayer, although his wife, Margueritte A. Evans, is also a petitioner since she filed joint returns with her husband for the taxable years involved.

notice of deficiency showing deficiencies in income tax for the two years in the amounts of $236.43 for 1962 and $1,089.35 for 1963. (R. 5-10.) Within 90 days thereafter, and on June 2, 1966, the taxpayer and his wife filed a petition with the Tax Court for a redetermination of the deficiencies under the provisions of Section 6213 of the Internal Revenue Code of 1954. (R. 1-11.) The decision of the Tax Court, entered September 22, 1967, found that there were deficiencies in the amounts of $41.21 for 1962 and $1,089.35 for 1963. (R. 88-89.) The case is brought to this Court by a petition for review filed November 13, 1967 (R. 90-91), within the three-month period prescribed in Section 7483 of the Internal Revenue Code of 1954. Jurisdiction is conferred on this Court by Section 7482 of that Code.

QUESTION PRESENTED

Whether the taxpayer, an owner and operator of a trailer park, is entitled to an investment credit (under Sections 38, 46 and 48 of the Internal Revenue Code of 1954) for the cost of four utility connections (for water, electrical energy, natural gas, and sewage disposal) used by those who rented space in the trailer park.

STATUTES AND OTHER AUTHORITIES INVOLVED

The pertinent provisions of the statutes and other authorities involved are set out in the Appendix, infra.

STATEMENT

The facts as stipulated by the parties (R. 16-19), found by the Tax Court (R. 66-69), and supplemented by the record may be summarized as follows:

In 1962, the taxpayer purchased Opal Cliffs Mobile Homes Park, having space for 111 trailers, for $327,000, of which $143,000 was the cost of the land, and $184,000 the cost of improvements of which at least $12,500 was the cost of each of four utility systems for the distribution of electrical energy, natural gas, water, and for sewage disposal. (R. 16-17, 67.) During the taxable years 1962 and 1963, the four utility systems were used in connection with the taxpayer's operation of the trailer park as follows (R. 17-19, 67-68):

(a) The sewage disposal system required no special attention and the charge for its use to each mobile home owner was made as part of the monthly charge for space. The system in Opal Cliffs Mobile Homes Park is connected to the East Cliff Sanitation District and is under the control of Santa Cruz County, California. (R. 17, 67.)

(b) The water in Opal Cliffs Mobile Homes Park was supplied by the C. L. Beltz Water System, a public utility operating under authority from the California Public Utilities Commission, Decision No. 20189. Each mobile home owner in Opal Cliffs Mobile Homes Park is charged $2.00 per month by the taxpayer as part of the monthly charge for space, in accordance with the schedule of rates established by the California Public Utilities Commission in their Decision No. 49269, for the sale of water by the C. L. Beltz Water System. The taxpayer in turn pays the C. L. Beltz Water System at a monthly rate which averages $50.00 per month. (R. 17-18, 68.)

(c) The taxpayer purchases all of the electrical energy used in Opal Cliffs Mobile Homes Park from Pacific Gas & Electric Company and pays for it at a fixed rate. The taxpayer, in turn, supplies the electrical energy to the mobile home owners in Opal Cliffs Mobile Homes Park and bills each mobile home owner in accordance with the amount of electrical energy used during the previous month. The taxpayer reads the meters each month, maintains appropriate records, and bills the mobile home owners for the amount of electrical energy used each month in accordance with a schedule of rates approved by the California Public Utilities Commission. (R. 18, 68.)

(d) The taxpayer operates a natural gas distribution system in the same manner as the electrical energy distribution system except that the California Public Utilities document which governs is "revised Cal. P.U.C. Sheet No. 5898G". (R. 18-19, 68.) The four systems had useful lives of 20 years for computing depreciation. (R. 68.)

On their original return for 1962, the taxpayer and his wife did not claim any investment credit (R. 20-31, 69), but on March 26, 1964, they filed an amended return for 1962, claiming the four utility systems as assets qualifying as property entitled to investment credit [2/] (R. 51-61, 69). The taxpayer's computation of total investment credit was $3,696.70, of which $1,152.11 was used to offset the income tax for 1962. (R. 61, 69.) An application of the

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2/ Investment credit was also claimed for other items not here in issue. The amended 1962 return reduced reported net profit by $442 because of adjustments not here in issue. (R. 26, 56.)

credit resulted in a claimed overpayment for 1962 of $1,239.63. (R. 62, 69.) The difference between the total claimed investment credit and the amount claimed in 1962 was carried over and claimed by the taxpayer as a credit to the extent of the full amount of the tax for 1963, or $1,136.34 (R. 32-47.)

SUMMARY OF ARGUMENT

The taxpayer is not entitled to investment credits in 1962 and 1963, under Sections 38, 46, and 48 of the Internal Revenue Code of 1954, for the cost of utility connections for water, gas, electric energy, and sewage disposal used by the tenants of a trailer park owned and operated by the taxpayer. The Tax Court correctly held that the statute, applicable Treasury Regulations and legislative history of the investment credit provisions of the Code clearly show that the taxpayer is not entitled to the claimed investment credit.

Code Section 46 provides for a credit against tax equal to a percentage of the investment in "section 38 property" which is defined in Code Section 48 to mean either tangible depreciable personal property, or "other tangible property" used as an integral part of manufacturing, production, or extraction, or furnishing transportation, communications, electrical energy, gas, water, or sewage dispoal services. The Treasury Regulations have reasonably interpreted the definition of "other tangible property" to mean that it is an integral part of furnishing the enumerated services by a person engaged in a trade or business of furnishing any such service.

The purposes of the investment credit provisions were to encourage investments by respective industries in furtherance of that business's

capital expansion and to encourage modernization and expansion of the Nation's productive facilities and to improve its economic potential. The legislative history further indicates that Congress was granting tax incentives to a supplier rather than a consumer of public utility property.

Code Section 46(c)(3)(B) provides that investment credit for certain public utility property is available only to one using the property who is predominantly in the trade or business of furnishing or selling the utility services. Utility property qualifies as "section 38 property" only when a public utility, predominantly in the trade or business of furnishing utility services, invests in service property to furnish services to the Community.

The taxpayer's returns reported his occupation as trailer park owner or trailer park operator. Those who rented trailer space from him received the utilities in question as an incident to the rental. He was not a public utility; he was not predominantly or otherwise in the trade or business of furnishing utility services; and he did not "furnish" utilities to his renters. The utilities were furnished by the companies from which the taxpayer obtained the water, electric energy, natural gas, and sewage disposal service. The taxpayer was merely a conduit from the terminal point of the distribution systems. He was a consumer rather than a supplier. There is nothing in the record to show that he did more than keep records and pay and collect bills. His utility connections in the trailer park did not fall within the broad purposes of the investment credit provisions of the Code.

ARGUMENT

THE TAXPAYER IS NOT ENTITLED TO AN INVESTMENT CREDIT UNDER SECTIONS 38, 46 AND 48 OF THE INTERNAL REVENUE CODE OF 1954 FOR THE COST OF UTILITY CONNECTIONS FOR WATER, GAS, ELECTRICITY AND SEWAGE DISPOSAL USED BY THE TENANTS OF A TRAILER PARK OWNED AND OPERATED BY THE TAXPAYER

The sole question on this appeal is whether four utility connections for water, electricity, gas, and sewage disposal service, used by renters of trailer spaces in a trailer park owned and operated by the taxpayer, qualify as "section 38 property" so as to permit the taxpayer to take an investment credit for the cost of such connections in 1962 and 1963. The taxpayer contends (Br. 16-23) that these four connections are "section 38 property" as "other tangible property" 3/ under Section 48(a)(1)(B), of the Internal Revenue Code of 1954, Appendix, infra, and, therefore, that he is entitled to investment credit under Section 38 of the 1954 Code, Appendix, infra. It is submitted that the Tax Court correctly held (R. 65, 70-80) that the statute, Treasury Regulations, and legislative history clearly show that the taxpayer is not entitled to the claimed investment credit. See Rev. Rul 66-269, 1966-2 Cum. Bull. 13-14, Appendix, infra.

Code Section 38 provides for a credit against tax equal to a percentage of the investment in certain eligible property known as "section 38 property". "Section 38 property" is defined in Code Section 48 to mean either (a) tangible depreciable personal property, or (b) other tangible property (not including a building or its

3/ No contention is made that the property in question qualifies as "Section 38 property" because it is "tangible personal property" under Code Section 48(a)(1)(A), Appendix, infra. It is clear from Section 1.48-1(c) of the Treasury Regulations on Income Tax under the 1954 Code, Appendix, infra, that electrical hookups, plumbing hookups, and oil and

structural components) if such property (i) is used as an integral part of manufacturing, production, or extraction, or of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services, or (ii) constitutes a research or storage facility used in connection with these activities. Under Section 1.48-1(a) of Treasury Regulations on Income Tax (1954 Code), Appendix, infra, other tangible property may qualify as "section 38 property"--

> only if such other property is used as an integral part of manufacturing, production, or extraction, or as an integral part of furnishing transportation, communications, electrical energy, gas, water, or sewage dispoal services by a person engaged in a trade or business of furnishing any such service, or is a research or storage facility used in connection with any of the foregoing activities, * * * (Underlining supplied.)

The validity of this section of the Regulations was upheld by the Tax Court as reasonable and consistent with the intent of the statute (R. 72-73), and the taxpayer does not here contend otherwise.[4/]

The purpose of the investment credit provision was to encourage investments by respective industries in furtherance of their capital expansion and "to encourage modernization and expansion of the Nation's productive facilities and to improve its economic potential * * *." See H. Conference Rep. No. 2508, 87th Cong., 2d Sess., p. 14 (1962-3 Cum. Bull. 1129, 1142); Madison Newspapers, Inc. v. Commissioner, 47 T.C. 630, 635. It is clear that the taxpayer's utility connections did not fall within the broad purpose of the investment credit provisions.

3/ (con't.) fall within the definition of "section 38 property" so as to qualify for investment credit as "tangible personal property." See also Rev. Rul. 66-269, 1966-2 Cum. Bull. 13, Appendix, infra.

4/ As the taxpayer's brief notes (p. 18), in the Tax Court he had unsuccessfully challenged the validity of the Regulations.

As the concurring opinion in the Tax Court pointed out (R. 78), the legislative history further indicates that Congress had in mind granting tax incentives for modernization and expansion to a supplier rather than to a consumer of public utility property. See, Detailed Explanation of the President's Recommendation Contained in his Message Taxation, 1 House Hearings before the Committee on Ways and Means on President's 1961 Tax Recommendations, 87th Cong., 1st Sess., pp. 256-257. Both the House and Senate Reports state, in language almost identical to the Regulations (H. Rep. No. 1447, 87th Cong., 2d Sess., p. A18 (1962-3 Cum. Bull. 405, 516) and S. Rep. No. 1881, 87th Cong., 2d Sess., p. 155 (1962-3 Cum. Bull. 707, 859)) that

> ***Property is to be considered as being used as an integral part of a system of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services only if such property is used by one engaged in the trade or business of furnishing such services. (Underlining supplied.)

An example is then given of a manufacturing firm which constructs an airstrip for use by airplanes operated for the convenience of its officers and employees, with the statement that such airstrip would not qualify as "section 38 property" since the manufacturing firm is not engaged in the transportation business. See H. Rep. No. 1447, supra, p. A18 (1962-3 Cum. Bull., p. 516), and S. Rep. No. 1881, supra, pp. 139, 155 (1962-3 Cum. Bull., pp. 843, 859).

Code Section 46(c)(3), Appendix, infra, provides that investment credit for certain public utility property is available only to one using the property who is "predominantly in the trade or business

of the furnishing or sale of electrical energy, water, or sewage disposal services." Section 1.46-3(g) of Treasury Regulations on Income Tax (1954 Code), Appendix, infra, after substantially repeating the words of the statute, states in part:

> ***If property is used by a taxpayer both in a public utility activity and in another activity, the characterization of such property shall be based on the predominant use of such property during the taxable year in which it is placed in service. (Underlining supplied.)

In other words, utility property qualifies as "section 38 property" only when a public utility, predominantly in the trade or business of furnishing utility service, invests in service property to furnish services to the community.

Section 1.48-1(h)(1)(ii) of Treasury Regulations on Income Tax (1954 Code), Appendix, infra, in excluding property used predominantly to furnish lodging or in connection with the furnishing of lodging from "section 38 property" eligible for the investment credit, states:

> ***Thus, such items as gas and electric meters, telephone poles and lines, telephone station and switchboard equipment, and water and gas mains, furnished by a public utility would not be considered as property used in connection with the furnishing of lodging. (Underlining supplied.)

Thus, in considering whether utility property qualifies for investment credit (notwithstanding the fact that it is a lodging facility or used in connection with the furnishing of lodging), the Regulations state it will qualify only where a public utility is using the property to furnish the services.

In this case, the taxpayer reported his occupation on his income tax returns (R. 20, 32, 51) either as "trailer park owner" or "trailer park operator." He rented space for trailers, and the renters of such space received the utilities in question as an incident to such rental. Contrary to the taxpayer's assertion (Br. 16-25), it is obvious that the taxpayer was not, predominantly or otherwise, in the trade or business of furnishing utility service, but made utilities available to his renters merely as an incidental part of his operation of the trailer park.

In fact, as the concurring opinion of the Tax Court points out (R. 78-80), the taxpayer was not "furnishing" the utilities to his renters at all. It was the C. L. Beltz Water System that furnished the water; the Pacific Gas & Electric Company furnished the electric energy and natural gas; and the East Cliff Sanitation District of Santa Cruz County furnished the sewage disposal system. The taxpayer merely acted as a conduit for them, obtaining as a consumer the water, electric energy, gas, and sewage disposal services from these suppliers, and then merely transmitting them to his renters of trailer space. The taxpayer was actually a consumer rather than a supplier, and merely acted as a conduit for the services from the terminal point of the distribution systems. The stipulated facts show (R. 17-19) merely that he read meters, maintained appropriate records, and billed the trailer owners for the various utilities they used. There is nothing to show that he did more than keep records and pay and collect bills.

The taxpayer, thus, was not a public utility, was not predominantly or otherwise in the trade or business of furnishing utility services, and, in fact, did not furnish the utilities in question at all. If the taxpayer's position were followed, every apartment owner who includes in the rent charged his tenants such items as water, electricity, gas, and sewage disposal, would be entitled to investment credit for the water lines, electrical, gas, and plumbing connections. The Commissioner's position is supported by Rev. Rul. 66-269, 1966-2 Cum. Bull. 13-14, where a taxpayer requested a ruling as to whether electrical hookups, and utilities used at a trailer park qualified for investment credit. In determining that they did not so qualify, the Commissioner pointed out (1) that such property was similar to oil and gas pipe lines which are considered real property[5/] (See H. Rep. No. 1447, supra, p. 12 (1962-3 Cum. Bull., p. 416): and (2) that the property failed to qualify as "other tangible property" used as an integral part of manufacturing, production, or extraction, or of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services, by a person engaged in a trade or business of furnishing any such service (see Code Section 48(a)(1)(B)(i) and Section 1.48-1(d) of Treasury Regulations on Income Tax (1954 Code), Appendix, infra.

5/ In the Tax Court, the taxpayer argued that the gas and electric meters were tangible personal property, but since the record contains no evidence of their cost as a separate item, nor any basis for an allocation, the Tax Court found it unnecessary to discuss the contention. The taxpayer has not raised the point on appeal.

It was unnecessary for the Tax Court to resort to Section 1.355-1(c) of the Treasury Regulations on Income Tax (1954 Code), as the taxpayer contends (Br. 18-21), and it did not do so. Code Sections 38, 46 and 48, the applicable Treasury Regulations, and the legislative history of the investment credit provisions, clearly show that the Tax Court properly denied the claimed investment credit in 1962 and 1963 for the cost of utility connections by which the renters of trailer space incidentally received water, gas, electricity, and sewage disposal services in the taxpayer's trailer park.

CONCLUSION

The Tax Court's decision was correct and should be affirmed.

Respectfully submitted,

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June, 1968.

CERTIFICATE

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

Dated: _____ day of _____ 1968.

_____
Carolyn R. Just

APPENDIX

Internal Revenue Code of 1954:

SEC. 38 [as added by Sec. 2(a), Revenue Act of 1962, P.L. 87-834, 76 Stat. 960]. INVESTMENT IN CERTAIN DEPRECIABLE PROPERTY.

(a) General Rule.--There shall be allowed, as a credit against the tax imposed by this chapter, the amount determined under subpart B of this part.

(b) Regulations.--The Secretary or his delegate shall prescribe such regulations as may be necessary to carry out the purposes of this section and subpart B.

(26 U.S.C. 1964 ed., Sec. 38.)

SEC. 46 [as added by Sec. 2(b), Revenue Act of 1962, P.L. 87-834, 76 Stat. 960]. AMOUNT OF CREDIT.

* * *

(c) Qualified Investment.--

* * *

(3) Public utility property.--

(A) In the case of section 38 property which is public utility property, the amount of the qualified investment shall be 3/7 of the amount determined under paragraph (1).

(B) For purposes of subparagraph (A), the term "public utility property" means property used predominantly in the trade or business of the furnishing or sale of--

(i) electrical energy, water, or sewage disposal services,

(ii) gas through a local distribution system,

(iii) telephone service, or

(iv) telegraph service by means of domestic telegraph operations (as defined in section 222 (a)(5) of the Communications Act of 1934, as amended; 47 U.S.C., sec. 222(a)(5),

if the rates for such furnishing or sale, as the case may be, have been established or approved by a State or political subdivision thereof, by an agency or instrumentality of the United States, or by a public service or public utility commission or other similar body of any State or political subdivision thereof.

* * *

(26 U.S.C. 1964 ed., Sec. 46.)

SEC. 48 [as added by Sec. 2(b), Revenue Act of 1962, P.L. 87-834, 76 Stat. 960]. DEFINITIONS; SPECIAL RULES.

(a) Section 38 property.--

(1) In general.--Except as provided in this subsection, the term "section 38 property" means--

(A) tangible personal property, or

(B) other tangible property (not including a building and its structural components) but only if such property--

(i) is used as an integral part of manufacturing, production, or extraction, or of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services, or

(ii) constitutes a research or storage facility used in connection with any of the activities referred to in clause (i)

Such term includes only property with respect to which depreciation (or amortization in lieu of depreciation) is allowable and having a useful life (determined as of the time such property is placed in service) of 4 years or more.

* * *

(26 U.S.C. 1964 ed., Sec. 48.)

Treasury Regulations on Income Tax (1954 Code):

§ 1.46-3 Qualified investment.

* * *

(g) Public utility property. (1) In the case of section 38 property which is public utility property, the amount of the qualified investment with respect to such property shall be 3/7 of the amount otherwise determined under this section with respect to such property.

(2) The term "public utility property" means property used predominantly in the trade or business of the furnishing or sale of--

(i) Electrical energy, water, or sewage disposal services,

(ii) Gas through a local distribution system,

(iii) Telephone service, or

(iv) Telegraph service by means of domestic telegraph operations (as defined in section 222(a)(5) of the Communications Act of 1934, as amended; 47 U.S.C., sec. 222(a)(5)),

if the rates for such furnishing or sale, as the case may be, have been established or approved by a State (including the District of Columbia) or political subdivision thereof, by an agency or instrumentality of the United States, or by a public service or public utility commission or other similar body of any State or political subdivision thereof. The term "established or approved" includes the filing of a schedule of rates with any body named in the preceding sentence which has the power to approve such rates, even though such body has taken no action on the filed schedule. For purposes of this paragraph, any activity described in subdivision (i), (ii), (iii), or (iv) of this subparagraph, which is regulated in a manner described in this subparagraph, shall be referred to as a "public utility activity". If property is used by a taxpayer both in a public utility activity and in another activity, the characterization of such property shall be based on the predominant use of such property during the taxable year in which it is placed in service.

* * *

(26 C.F.R., Sec. 1.46-3.)

§ 1.48-1 Definition of section 38 property.

(a) In general. Property which qualifies for the credit allowed by section 38 is known as "section 38 property". Except as otherwise provided in this section, the term "section 38 property" means property (1) with respect to which depreciation (or amortization in lieu of depreciation) is allowable to the taxpayer, (2) which has an estimated useful life of 4 years or more (determined as of the time such property is placed in service), and (3) which is either (i) tangible personal property, (ii) other tangible property (not including a building and its structural components) but only if such other property is used as an integral part of manufacturing, production, or extraction, or as an integral part of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services by a person engaged in a trade or business of furnishing any such service, or is a research or storage facility used in connection with any of the foregoing activities, * * *

* * *

(d) Other tangible property--(1) In general. In addition to tangible personal property, any other tangible property (but not including a building and its structural components) used as an integral part of manufacturing, production, or extraction, or as an integral part of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services by a person engaged in a trade or business of furnishing any such service, or which constitutes a research or storage facility used in connection with any of the foregoing activities, may qualify as section 38 property.

* * *

(3) Transportation and communications businesses. Examples of transportation businesses include railroads, airlines, bus companies, shipping or trucking companies, and oil pipeline companies. Examples of communications businesses include telephone or telegraph companies and radio or television broadcasting companies.

(4) Integral part. In order to qualify for the credit, property (other than tangible personal property and research or storage facilities used in connection with any of the activities specified in subparagraph (1) of this paragraph)

must be used as an integral part of one or more of the activities specified in subparagraph (1) of this paragraph. Property such as pavements, parking areas, inherently permanent advertising displays or inherently permanent outdoor lighting facilities, or swimming pools, although used in the operation of a business, ordinarily is not used as an integral part of any of such specified activities. Property is used as an integral part of one of the specified activities if it is used directly in the activity and is essential to the completeness of the activity. Thus, for example, in determining whether property is used as an integral part of manufacturing, all properties used by the taxpayer in acquiring or transporting raw materials or supplies to the point where the actual processing commences (such as docks, railroad tracks and bridges), or in processing raw materials into the taxpayer's final product, would be considered as property used as an integral part of manufacturing. Specific examples of property which normally would be used as an integral part of one of the specified activities are blast furnaces, oil and gas pipelines, railroad tracks and signals, telephone poles, broadcasting towers, oil derricks, and fences used to confine livestock. Property shall be considered used as an integral part of one of the specified activities if so used either by the owner of the property or by the lessee of the property.

* * *

(h) Property used for lodging--(1). In general. (i) Except as provided in subparagraph (2) of this paragraph, the term "section 38 property" does not include property which is used predominantly to furnish lodging or is used predominantly in connection with the furnishing of lodging during the taxable year. * * * The term "lodging facility" includes an apartment house, hotel, motel, dormitory, or any other facility (or part of a facility) where sleeping accommodations are provided and let, * * *

(ii) Property which is used predominantly in the operation of a lodging facility or in serving tenants shall be considered used in connection with the furnishing of lodging, whether furnished by the owner of the lodging facility or another person. Thus, for example, lobby furniture, office equipment, and laundry and swimming pool facilities used in the operation of an apartment house or in serving tenants would be considered used predominantly in connection with the furnishing of lodging. However, property which is used in furnishing, to the management of a lodging facility or its tenants, electrical energy, water,

sewage disposal services, gas, telephone service, or other similar services shall not be treated as property used in connection with the furnishing of lodging. Thus, such items as gas and electric meters, telephone poles and lines, telephone station and switchboard equipment, and water and gas mains, furnished by a public utility would not be considered as property used in connection with the furnishing of lodging.

* * *

(26 C.F.R., Sec. 1.48-1.)

Rev. Rul. 66-269, 1966-2 Cum. Bull. 13:

Advice has been requested whether certain assets used at a trailer park qualify for the investment credit. Specifically, the property in question includes electrical hookups, plumbing hookups, and water wells.

Included in the costs of plumbing hookups are the surveyor fees, the digging of trenches, the installation of water and sewer pipes, the construction of a mound of rocks as a drainage field, septic tanks for dumping on the drainage field. The electrical hookups include the costs of lead-in wires from the utility poles, which were installed throughout the trailer park, the costs of hookup boards, fuse boxes, and plug-in units. The cost of water wells include the actual drilling, the well casings, and electric pumps.

Section 48 of the Internal Revenue Code of 1954 provides, in part, that for property to qualify as "section 38 property" for which an investment credit is allowed, it must be either (1) tangible personal property or (2) other tangible property (not including a building or its structural components) used as an integral part of manufacturing, production, or extraction, or as an integral part of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services.

"Tangible personal property" is defined in section 1.48-1(c) of the Income Tax Regulations to include all tangible property except land and improvements thereto, such as buildings or other inherently permanent structures (including items which are structural components of such buildings or structures). In addition, all property which is in the nature of machinery (other than structural components of a building or other inherently permanent structure), shall be considered tangible personal property even though located outside a building. Thus,

for example, a gasoline pump, hydraulic car lift, or automatic vending machine, although annexed to the ground, shall be considered tangible personal property. Furthermore, H.R. Report No. 1447, Eighty-seventh Congress, second session, C.B. 1962-3, 405, at 415, states that tangible personal property is not intended to be defined narrowly, nor necessarily to follow the rules of State law. Although assets accessory to a business such as grocery store counters, printing presses, etc., are to qualify for the credit, the same Committee Report, at page 416, specifically considers property such as oil and gas pipelines and fences to be real property.

The electrical hookups, plumbing hookups, and water wells are in the nature of land improvements, similar to oil and gas pipelines which are considered as real estate. Only the electric pumps used in connection with these facilities qualify as tangible personal property.

"Other tangible property," as defined in section 1.48-1(d) of the regulations, is property used as an integral part of manufacturing, production or extraction, or as an integral part of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services by a person engaged in a trade or business of furnishing any such service. The properties in question do not qualify under this definition.

Accordingly, electrical hookups, plumbing hookups, and water wells, except for the electric pumps used in connection therewith, installed at a trailer park are not "section 38 property."